Brookings-CIGI-G24 High Level Seminar

Delivering on IMF Quota and Governance Reform
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Past Commitments and Future Reforms

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I will speak about both what I call "Representational" IMF governance as well as "Internal" Fund governance.

First on Representational IMF governance. The most important aspects of this are obviously quotas and voice of members of the institution. The reforms under way are important and will hopefully go some distance to help rectify the imbalances that developed over the last decades. But, in my view, the reforms made to date are disappointing. There remain major problems with the way in which the Fund is governed at the highest levels - by which I mean at the level of the G7 and, more recently, at the level of the G20. And that impacts the power of individual members beyond what they may have through quota and voice.

As some of you know, I have not been a fan of the G20. Surely it was an advance over the G7 by increasing the number of countries involved and by regularizing meetings at the Leaders level. It proved its worth in the early stages of the financial crisis in 2008 and 2009 which saw a remarkable - if short lived - period of intense global cooperation. It has also served to push forward some of the more important reforms needed in the IMF. This latter, however, has been a mixed blessing - as I'll discuss later.

Some would also argue that the G20 has put in place important mechanisms - such as the Mutual Assessment Process (MAP) - to help foster what the original announcements about the process said would be "strong, sustainable and balanced

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growth". But I see a number of problems with that process - problems that both hinder its effectiveness and, in my view, weaken the Fund. It's that latter concern - and its relation to Fund governance - that leads me to spend a few moments on the issue. It appears to an outsider like me that what should have been a process aimed at a single, broad objective - essentially finding complementary and reinforcing growth paths for all the major countries, seems to have become, since the Seoul Declaration, focused solely on "...promoting external stability" and "...reducing external imbalances". Growth seems to have fallen off the screen!

In some other ways the MAP may be an advance on the multilateral consultation process (MC) as it ultimately involves the G20 Leaders whereas the MC engaged less senior officials. The MAP has also introduced "indicative quantitative guidelines" against which performance - such as the sustainability of current account imbalances - can be assessed. That could be a useful beginning of the broader use of what The Palais Royal Initiative Report called "norms" for member policies - essentially quantitative alarm signals to put more teeth into the surveillance process.[2]

However, I believe that the MAP process is flawed. The multilateral consultation process that was attempted in 2006/2007 was at least structured with the IMF in the role of *lead facilitator* and with reports prepared by staff to be formally discussed by the executive board before they were released to the public. But the MAP, as I understand it, puts the Fund staff in the role of technical advisor, with the G20 members determining the inputs to be sought from the staff. Moreover, since the entire process is considered to be "technical assistance", it leaves publication of any analysis done by the staff in the purview of the G20. Among other things, I see this as a retreat from the Fund's otherwise laudable progress on transparency.

In short, I believe it is unhelpful for the Fund staff's work with the G20 on the MAP to be conducted under the Fund's policies that guide technical assistance. Rather, that work should be done under the Fund's normal - but strengthened - surveillance policies. If that were the case, the Fund could provide the support needed by the G20 and the G20 could lead the way in finding ways to make IMF surveillance what it ought to be for all member countries, rather than the generally weak mechanism it has proven to be to date. If there is to be serious accountability on members to comply with their obligations under the Articles, Fund surveillance has to be significantly strengthened - and no more importantly than in the case of countries

[2] See "Reform of the International Monetary System: The Palais Royal Initiative" edited by Jack Boorman and Andre Icard, Sage Publications, 2011. The Palais Royal Report appears on pages 7 - 26.

such as those that comprise the G20. Thus, if the MAP continues, I believe that the process needs to be reformed.

More broadly, my fundamental problem with the G20 stems from its membership and from its effective exclusion of 168 IMF member countries. In a paper published by Brookings in 2007, I attempted to lay out some principles to guide the development of better global governance structures.[3] The main principles I suggested included Universality, i.e., the inclusion of all countries in the global economic and financial decision-making structure; Legitimacy - or what might be described as simple fairness; Subsidiarity, i.e., making decisions as close to the ground, and as close to those affected, as possible, but within a broader framework agreed at a more global level. I added also Efficiency; and Accountability. Obviously the G20 is neither universal nor does it satisfy the norms of subsidiarity. The Group's legitimacy and accountability - to whom or to what - is also unclear.

The country membership of the G20 is also problematic. Those of us involved at the time - in the wake of the Asian crisis - recall that the decision on which countries to include was heavily influenced by the aftermath of that crisis and by the personalities that were in power in certain countries who would represent the countries selected. The result is a group of countries that represents a large share of the global economic and financial system, but some of which could hardly be seen as role models for other countries looking for examples to help them maneuver through the increasing complex global system. Beyond that, there appears to be no mechanism to change or rotate membership.

Any reform of global economic and financial governance must start with reform of the G20. Of course, the membership issue can only be decided at the highest political level. On the other hand, the failure of the G20 to be inclusive and universal, and its capacity to promote subsidiarity can be resolved. In my view, the solutions lie in basing the Group on a constituency system, and exploring the possibility of building that system on the regional financial groupings that have emerged over the last couple of decades. This too was a recommendation of the Palais Royal Initiative. There are multiple regional forums, but it is not clear that they build in a coherent fashion to a system that facilitates effective representation within the small Groups - the G7 and the G20 . What is needed are more effective vehicles through which the views put forward and the positions taken in those regional financial forums can

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[3] IMF Reform: Congruence with Global Governance Reform, published in Global Governance Reform: Breaking the Stalemate, Colin I Bradford, Jr. and Johannes F. Linn, editors,. Brookings Institution Press, 2007, pp. 15 - 31.

effectively percolate up to the predominant Group. Strengthening relations with regional economic and financial groupings can also help provide a rich source of information "on the ground" so to speak.

The obvious relevant example of a working constituency system is the IMF executive Board. And the obvious place to have meetings of Finance Ministers and Central Bank Governors playing the role being played by those officials in the G20 is in the IMF. That leads to a proposal to merge the G20 and the International Monetary and Financial Committee (IMFC) into a single body. Such a structure would have the virtue of employing a constituency structure similar to that of the IMFC and the Fund executive board. The size of the Group may be an issue. I understand that the agreement reflected in the Seoul Declaration of the G20 - and endorsed in the Fund - is to keep the executive board at 24 members - all of whom are to be elected. Thus the size of a group to replace the G20 might initially need to be of that size. But this is an issue that could perhaps be revisited. Whether such a Group should be formed as a Council, as favored by Michel Camdessus and which I support, is an open question for another day, and not a necessary element of the proposal.

The timing for this proposal is auspicious. The executive board has been asked to complete its reform of the composition and structure of the board to reflect the new quotas - which are to take affect by the 2012 annual meetings in October - and to accommodate the fact that all Executive Directors are to be elected no later than the subsequent Board election, which I assume will be in November. I realize that most reform in the international community moves somewhat slower than the melting of the ice in glaciers. But since that's speeding up, perhaps a reform as important as the merging of the G20 and the IMFC could also be accelerated.

Given the other reforms that are to follow - such as the comprehensive review of the quota formula and the completion of the next general review of quotas by early 2014 - this merging of the G20 Ministerial and the IMFC is urgent. It is important that the experience of the past several years, when critical decisions regarding the IMF were effectively taken in the G20 and brought into the IMFC and the Fund to be formalized, not be repeated. That process weakens members' sense of ownership and challenges the concepts of universality and legitimacy when a small Group such as the G20 brings an idea into the Fund that has been too finely tuned and cannot be subject to genuine debate and modification. In the end, such a practice also blurs the issue of accountability. Only involvement of all the membership through a constituency system - preferably related to the structure and membership of regional financial groupings, will produce this result. All members must feel that they have a say in the

most important issues confronting the institution. Only that will produce the all-important sense of ownership required for the Fund to operate more effectively.

<u>2. Internal or Managerial Governance.</u>

Under this heading, I would include:

- **The selection process for the MD and the DMDs;**
- **The management structure; and**
- **Selection of the Dean of the Board**

I'll briefly make just a few points on each of these issues.

The process through which the MD is selected has been under discussion for years - and there has been some progress. But the process is, in my view, still flawed.

Will the European and U.S. stranglehold on the Fund and Banks leadership posts ever be broken? Some of us were hopeful for a change away from Europe 10 years ago, and 7 years ago, and 5 years ago and last year. Alternative candidates have been put forward, but the result has been always the same.

I believe two things need to be done to break the circle.

- First, there should be a public commitment from both Europe and the U.S. not to put forward candidates for the next vacancy that arises in the respective institutions. Only opening the field in that way will avoid a repetition of the same results again and break the tradition the has co-opted the positions for far too long. I recognize the political challenge this represents - especially with elections looming in so many countries in the next year or so!

- Second, the process needs to be further reformed. I believe that some of the transparency recently achieved needs to be re-thought. Greater transparency is almost always good. But there is a problem with too much transparency in the selection process. It derives from a simple fact: some of the candidates that would be the very best for the jobs are likely to be reluctant to have their names put into a hat and find themselves publicly rejected. This means that the institutions may well not get the very best leadership that is available. Corporations, universities and other organizations deal with this issue and they have found ways to quietly sound out the preferred candidates in a manner that avoids the loss of face that can come with

rejection. It should be possible to find a way to do that for the Fund and Bank leadership positions as well.

The selection of DMDs faces its own problems. The position of FDMD has always gone to a U.S. national. Two of the other three positions appear to have been captured by specific nationalities. There is also a question of the extent to which the MD's views and preferences should be taken into account in the selection of DMDs. There have been examples of excellent teams being formed under the current selection processes. But there have also been periods of clear dysfunctionality in management, resulting, in part, from personality clashes. I believe that is no secret. There is a case to be made here to get expert, outside advice on these issues to better the experience in team leadership

Also on this issue, I consider Department Heads to be part of "management". But that is not the way the term is used in the Fund. In my view, the creation of multiple DMD positions has caused a diminution in both the role and the image of department heads. I believe the managerial structure of the Fund needs to be re-thought. I also believe outside expertise could help in thinking through this issue.

The response to suggestions like this has often been "the Fund is unique and those outside do not understand the culture and workings of the institution sufficiently well to contribute substantively to these issues." I don't believe that. It would not be that expensive to at least test this proposition by calling in a noted firm with expertise in these areas to hear their recommendations.

Further on management issues: it seems that almost every evaluation done by the Fund's Independent Evaluation Office (IEO) and by others regarding some aspect of IMF operations concludes that there is a pervasive "silo" mentality in the institution that limits its effectiveness. I believe it is well past the time to address this issue more frontally than has been done to date.

My last point on this managerial structure issue goes to the position of Dean of the Executive Board. I recognize that it has been a long tradition in the diplomatic community for the longest serving ambassador to serve a Dean of the diplomatic community. That may work in that community, but I believe it to be an inappropriate model for the IMF Board. The position of Dean has become increasingly an executive position with the increase in the number of board committees and some devolution of power to those committees. It is also my view that the Dean should be, and be more visibly seen as, a leader of the board. This, of course, raises issues about the relationship between the Dean as a leader of the Board and the MD as Chair of the

board. But there are other reasons to re-examine the role of the MD as Chair of the board. I suggest that these issues too deserve study. The Dean, in my view, should be elected by the board with only some constraints - such as time already served on the board - and should be subject to a specific term. There are other models as well that could also be considered. It would be important to consider the capacity of any candidate for Dean to work effectively with the MD, in particular.

Let me say, please, that none of what I am saying is meant to reflect on the personalities of any individuals who have held or are holding the positions that I have mentioned! These are structural issues.

The reforms needed to the Fund are many and complex. There is no better time to focus on the needed reforms than now - when the world is reassessing the future place of the institution in the global system in light of the repeated crises seen in the most developed countries in the past five years.